

THE BLACK MARKET PESO EXCHANGE: HOW U.S. COMPANIES ARE USED TO LAUNDER MONEY

HEARING

BEFORE THE

SENATE CAUCUS ON INTERNATIONAL NARCOTICS CONTROL

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Senator SESSIONS. So the Colombian government is making some successful steps toward making it more difficult to launder these funds?

CARLOS. Oh, yes, yes, they are.

Senator SESSIONS. And but ultimately you believe the black market will continue. I believe you said to stop this problem, it will be necessary for the government of Colombia to reduce these ridiculously high tariffs and taxes. Do you think it will continue as long as you have a 60 percent tax in effect on imported goods?

CARLOS. Yes, I heard that Ms. Fanny Kertzman and maybe it will help her what I am going to say. In Colombia, when you import something, right off the bat, you have a 16 percent tax, sales tax, plus the tariffs, plus a lot of other expenses and plus a lot of other paperwork. If you really want to stop the black market, you can do it I will not say today, but if you reduce drastically those tariffs and the taxes, it will last about a month, and everybody would become legal.

Senator SESSIONS. There would not be any advantage to being illegal; is that correct?

CARLOS. Yes. What I am going to say is going to sound a little awkward, but these contrabandistas are legit businessmen. Okay. They buy the funds. I understand this. But they are not, they would rather do legit business than what they are doing now. Now it is uncomfortable and these are people who want to make a living importing merchandise. If the tariffs went down, like in the United States, you do not have cars smuggled in or textiles. Your tariffs, I suppose they are very low. So it is not worth it to smuggle anything in. So if the tariffs and taxes were lower, nobody will go through the hassle of trying to bribe a Customs officer or anything like that.

Senator SESSIONS. Thank you very much for providing us this rare insight into how this business actually occurs, Mr. Chairman, and, Carlos, we thank you for sharing it with us and I understand the need for the security and we thank you for coming.

CARLOS. Thank you. Yes.

Senator GRASSLEY. One last thank you and would you please stay seated until we know that everything is all right. And I think the cameras should be a little more cautious about being turned off or turned away from the witness. I do not think they were when we brought the witness in and I would like to have respect for his security. Even though he is hooded, it is still very important that we do that. So when the police say that it is okay to proceed, then we will proceed and when you are out, then I will introduce our fourth and last witness. Is it okay to proceed now? I want to thank all in our audience for your cooperation for the safety of Carlos.

FOLLOWUP QUESTION FOR "CARLOS"

In your testimony, you mention various companies that do business in the Black Market Peso exchange. Could you list these companies that have received funds, and mention some of the items that are sold?

Carlos supplied the following list:

Companies: Sony; Whirlpool; Kodak; General Electric; Madame Shikse & CIALTD; Caja Agraria; Comercializadora Siglo XXILLDA; Multicentro Del Blumer C.A.; Surtibhumer C.A.; Motorola; Aiwa Electric; and Toshiba.

Goods: Scotch (Black Label-Johnny Walker brand); Marlboro Cigarettes; Johnson and Johnson; Mattel Brand Toys; Cell Phones (manufacturers Erickson and Nokia); Emerson; Perfume; and Patton Ceiling Fans.

Senator GRASSLEY. Our fourth and final panel consists of Ms. Fanny Kertzman, Director General of Taxes and Customs for the Government of Colombia, and also we have another witness, former U.S. Ambassador to Venezuela, Michael Skol. Mrs. Kertzman was recently appointed by President Andres Pastrana and I welcome her and thank you for your courage in appearing before the caucus today, and Ambassador Skol, you served as ambassador from 1990 to 1993 and you are currently president of Skol and Associates, a consulting firm here in Washington, D.C.

And before you begin, Ms. Kertzman, I want to thank your ambassador who was here for a short period of time this morning for his interest in this issue not only for today's appearance but also because he has expressed concern over these very issues so many times that he has visited my office and we very much appreciate your president's interest in this issue, his cooperation with our country, his trying to make very substantive changes within his own country, but also I think the presence of your ambassador on these issues before members of Congress is an appreciation or an expression of that as well.

And my staff reminds me that I pronounced your name wrong. Mr. Skol.

Mr. SKOL. Thank you, sir.

Senator GRASSLEY. You bet. Ms. Kertzman, would you proceed, please.

STATEMENT OF HON. FANNY KERTZMAN, DIRECTOR GENERAL OF TAXES AND CUSTOMS, GOVERNMENT OF COLOMBIA

Ms. KERTZMAN. Thank you very much. I want to thank the Senate Caucus on International Narcotics Control and especially your chairman, Senator Charles Grassley, Senator Sessions, for the opportunity to address one of the most serious problems facing Colombia which is contraband. The government of Andres Pastrana has made a point of his fight against corruption in general and one of the most important points is the fight against contraband. Contraband in Colombia amounts to near \$5 billion a year, which means with a total import of \$15 billion a year, it means that almost 25 percent of all the imports that are made into Colombia are contraband.

And the reason for that is not that the taxes are very high. We lowered our taxes on imports in 1992 and what happened is that contraband raised by the result of opening the economy and I think that the main reason for this huge amount of contraband into the country is mainly the narcotics trafficking. The problem of narcotics trafficking is not only a problem of the U.S. or only a problem of Colombia. It is a problem for all of us. For Colombians, we have the harm that is done to our youth just the same as here in the U.S., but in Colombia, we have the problem of corruption, contraband, the danger that people are—you were asking now this other witness about the danger that people are in in Colombia. It is not only the judges, the policemen, the army, it is also us officials of Colombian government that we have to go protected. I have

about nine guards. My family has about six guards and it is only because we are fighting against contraband and tax evasion.

It costs, contraband costs to the Colombian state, each year about \$840 million in tax revenue and duties that are not paid. And why there is such a high contraband is not to pay duties so to make unlawful competition to the other producers in Colombia, but also to launder money as I said. Also there is contraband of chemical precursors and the contraband of the point of view of export of illegal substances.

The link between narco-trafficking and contraband is very clear. This merchandise that is smuggled into Colombia is bought with an exchange rate for the dollar of 1,000 pesos per dollar when the rate in the market is 1,600 pesos per dollar. That is why it is such a good business to smuggle goods into Colombia and it adds to the profits of the narco-traffickers. I have to stress the point that the dirty dollars are not deposited in Colombian banks. They, you just heard all the explanation of how it works, but I want to make clear that in Colombia, it is not possible to open an account in dollars, only in pesos.

The dollars that come into Colombia sometimes come dollars in cash. When we caught dollars in cash, it is about \$300,000 every time they are caught at the airports with people, in their luggage or taped to their bodies, but that is not the most common way of laundering the profits of narcotics. All the actors in the chain of contraband are accomplices to this crime. The producer, the manufacturer of the goods here in the U.S. or in Japan or in Korea, who knows that he is selling the goods to someone that finally will smuggle them into Colombia.

The distributor who is selling the goods to the smuggler, the peso broker, the smuggler itself and the consumer in Colombia who buys the smuggled goods know that the product he is buying was paid with money from narco-traffickers. All of them are equally guilty of the same crime, that they are selling goods that are going to be smuggled into Colombia and paid with dirty money.

With all these problems we have with contraband, I would like to stress that we are working very closely with U.S. government. We have received all the cooperation that we need, especially from the U.S. Customs Service, the Department of the Treasury, Department of Justice, DEA, FBI, FinCEN, OFAC, and in general the agencies that somehow are related to this issue. We are signing an agreement with Customs. It is all ready for the signature and I think it is going to be signed on September that will be interchange of information between U.S. Customs and the Colombian Customs and we are working together with them already in the cases, the specific case of contraband and money laundering.

For the first time in Colombia, there are people in jail for contraband. Contraband is a crime and tax evasion is also a crime in Colombia, but there is no one in jail for tax evasion. Now in Colombia there are about 20 or 22 people in jail for a case of contraband and for you it might be a very low figure, but for Colombia it is a record to have 22 people in jail for contraband.

There also has been some progress with the private sector. We are trying that the private sector be aware that they cannot sell their goods to smugglers and there are some companies such as

Whirlpool Corporation and Daewoo in Korea that have as a policy not to sell to the contrabandistas. And Whirlpool Corporation just signed a compliance agreement with the government of Colombia that they are not selling through the distributors in Miami and in Panama. They are selling only one unit of every dishwasher or something like that, and Daewoo has a policy not to sell to the Sanandresitos in Colombia.

For those who are not aware what the Sanandresitos are, this is our big malls that exist in Colombia where they sell only smuggled goods. There are Sanandresitos in every major city in Colombia. People go to buy appliances and liquor, cigarettes; it is much cheaper than in the legal market, of course, because they are not paying taxes. They are very well organized and it is a phenomenon that I think it exists only in Colombia.

There are cases of contraband that are very clear. The case of tobacco, for example. Nearly 90 percent of the total of cigarettes imported into Colombia are contraband. Local companies have 55 percent of the market. 45 percent of the market is imported cigarettes. Only ten percent of them are imported legally. 90 percent of all the cigarettes that come into Colombia are contraband. In the case of liquor, 85 percent of the total liquor that is imported in Colombia is contraband.

Six years ago there were 18 legal distributors of imported liquors in Colombia. Now only three of them remain. They went into bankruptcy because of the unlawful competition of contraband. For Colombia, it is a problem the Colon Free Trade Zone located in Panama. The Panamanian government has been very reluctant to provide figures regarding exports from the free zone, but in Colombia, we estimate that \$1.2 billion a year come from the Colon Free Trade Zone illegally into Colombia. The Sanandresitos buy their goods mainly in the Colon Free Trade Zone.

We are trying to work together with U.S. government in this fight against contraband. We are asking for funds to buy X-ray machines for the ports and the airports. They do not exist. We want to work together with the U.S. government, but I want to say again that contraband is not a problem only in Colombia. Such as drug trafficking, the problem is international problem, not only a problem of U.S. and Colombia, but all the countries. I just want to end by saying that contraband is the second stage of narco-trafficking. It is the most efficient way of money laundering and from that point of view we together have to work on this. Thank you very much.

[The prepared statement of Ms. Kertzman follows:]

Contraband, Money Laundering, and Peso Brokerage

Fanny Kertzman

Director of Revenue and Customs Service

Government of Colombia

I would like to thank the members of the Caucus on International Narcotics Control and, specially, your Chairman, Senator Charles Grassley, for the opportunity to present one of the most serious problems of my country: **contraband.**

My name is Fanny Kertzman, I am the Director of the Revenue and Customs Service in Colombia, DIAN. I assumed this position in August of 1998, when I was appointed by the current President, Andres Pastrana. The institution that I direct is dedicated to guaranteeing the compliance of tax and customs obligations by my countrymen, and to facilitate the operations of international trade.

The DIAN is an entity of the Ministry of Finance and, therefore, develops the policy and programs of the central government. One of the main priorities of the current government is to combat tax evasion and contraband. My Directorate coordinates efforts of the other entities of the government in the fight against contraband.

Although contraband has been a constant phenomenon throughout Colombia's history, over the past few years it has become one of the main scourges, a source of destabilization and, particularly, has adversely affected the country's productive sector. Because of contraband, millions of Colombians have lost their jobs, to the extent that the unemployment rate in Colombia is close to 19.5%, which was undoubtedly exacerbated by the unlawful competition sponsored by this phenomenon.

It is ironic that although Colombia has substantially reduced import tariffs and now has an average tariff close to 8.7%, contraband has increased instead of decreased. This is only explained if we take into account the relationship between contraband and other big problems that threaten my country: **narcotrafic and money laundering.**

Contrabands' impact on commercial, industrial and job generating activities has been devastating, specially in recent years, when its links with drug traffic and money laundering have been more than evident.

Contraband in Colombia is of unimaginable magnitude and has been quantified by varying estimates. Some have calculated that open contraband accounts for US\$2.5 billion dollars per year; and that technical contraband and under-invoicing amounts accounts for an equal value, which adds up to a total contraband figure of US\$5 billion. Compared to total imports in 1998 amounting to US\$15 billion, the result suggests that contraband accounts for 25% of legal imports. In terms of GDP, contraband ranges between 2% and 3.5% of Colombian GDP.

The economic costs are extremely high, not only from the standpoint of jobs lost to unlawful competition, but also due to the tax revenue lost by the State. According to recent estimates of the DIAN, in 1998, open contraband amounted to US\$2.3 billion. With an effective 16.6% tax rate (for VAT and Duty), the losses to the national treasury during last year could exceed US\$390 million. This does not take into account technical contraband, through which merchandise is smuggled under a different tariff heading in order to pay fewer taxes; nor under-invoicing, where lower prices are invoiced to reduce taxation, as well. Of a total contraband estimate of US\$5 billion, annual fiscal losses in 1998 accounted for US\$840 million, although this figure could be an overestimate, as technical contraband and under-invoicing pay a certain amount of taxes, unlike the case of open contraband.

54.1%, on average, of the Nation's ordinary income over the past few years has been transferred by the National Government to provinces in the form of fiscal transfers and municipality shares. Therefore, departments, municipalities, and Indian reservation have lost earnings amounting to US\$454 million on account of contraband, which has affected the supply of basic services to Colombia's population in the areas of education, health, water, and basic sanitation, recreation and sports, and other social investment funds to be allocated locally.

In the opinion of renowned experts, money laundering and drug traffic are the most decisive factors, as large profits derived therefrom lead to a dollar price well below the price paid by legal importers, a fact that leads to unfair and disturbing competition for the market of foreign goods.

1. The Chain of Contraband and Money Laundering

In Colombia, contraband is an established business. In open contraband, goods are smuggled to avoid taxation, to launder moneys earned illegally through drug traffic, to import raw materials for drug traffic (chemical components); and to feed the war through weapon contraband.

It cannot be denied that all elements of the contraband chain, such as the manufacturer, transporter, distributor, retainer, peso broker, and even the consumer contribute significantly to the entire process.

The mechanism, in the case of drug traffic money laundering, is the following:

1. Producers in different countries, such as the United States, England, Korea, Japan and China, sell their merchandise to distributors located in Miami, Los Angeles, Panama, Aruba and other Caribbean countries.
2. Colombian smugglers purchase the merchandise from these distributors or, in some cases, directly from the manufacturers.
3. The smugglers are contacted by peso brokers who provide the dollars, supposedly earned through drug traffic, to pay their suppliers.
4. It is assumed that these dollars are derived from drug traffic, as they are sold at a significant discount compared to the official prevailing price in Colombia (Col.\$1,000 against Col.\$1,650).
5. The smugglers deposits in Colombian peso accounts the equivalent to the sum paid in dollars to the supplier. Here, it is worth pointing out that in Colombia there are no bank accounts in dollars. This means that the dollars do not enter Colombia, but rather are paid to the suppliers in the United States, Panama, Aruba, or Caribbean countries.

The Colombian government believes that many of the multinational companies perfectly know the mechanism described above and are aware of the fact that their products finally enter Colombia. Consequently, the government intends to develop among these companies a "know your client" campaign, as the one operating in the financial sector, to prevent multinational companies from selling their products to distributors who are suspected of being involved in the money laundering scheme.

The US Government has understood this initiative. It is necessary to create an awareness of the fact that any member of this criminal chain, from the

manufacturer in a foreign country to the buyer in the streets of Colombia, may be an accomplice, either by action or omission.

Another link in the chain is the Colombian customs official, who receives bribe from smugglers. Drug traffic moneys have permeated practically every level of Colombian society. Part of the drug traffic chain are the peso broker mechanism and the smugglers. Contraband is not limited to fiscal losses and unlawful competition. It also has serious consequences on the moral of society, on values, on the perception of what is legal and what is not. Contraband is the cause of corruption problems in the Colombian customs authority, which lead to official rotation and hinders proper training and lasting jobs, as well as demoralizes honest officials, and worse yet, even produces death threats.

Over the past year, two Colombian customs officials were assassinated. In one case, it was because a female customs agent refused to allow a shipment of weapons and military uniforms to be smuggled into the country, which meant her death sentence.

Money laundering does not only occur in the context of contraband. Constantly shipments of dollars are seized, which are introduced illegally into the country. During the last three months of 1998, nearly US\$300,000 were seized every week from travellers entering the El Dorado Airport in Bogotá. It is also common for shipments of contraband goods to carry dollars hidden inside electronic appliances.

Hence the need to have X-ray equipment in all customs checkpoints in the country. At present, no port of entry has this type of equipment. We are requesting the US Congress and the US Government to donate this equipment to the country. This would contribute to control contraband, dollar laundering, as well as the entry of chemical precursors and export of illegal drugs. US Customs Service is going to provide technical assistance to assess the actual needs for this equipment and the specifications required to meet Colombia's customs needs.

2. Contraband: An International Cooperation Issue

In spite of control activities developed by the customs authority, the achievements have been scarce vis-à-vis the magnitude of this phenomenon. Last year, only US\$153 million in merchandise was seized, which reveals the impotence of Colombian authorities faced with contraband. This figure accounts for merely 6% of total contraband.

The Pastrana Administration has received strong support from the US Government in various forms that are described below.

The creation of cooperation agreements for customs-related issues with other countries is an efficient tool for obtaining information in development of investigations and to procure technical assistance for purposes of improving control procedures. Such is the case of the agreement to be signed shortly between the US Customs Service and Colombian Customs Authorities.

This agreement provides for exchange of information, cooperation, training, technical assistance, and joint investigation of contraband and money laundering cases.

Furthermore, the Colombian government has received assistance and aid from the Department of Justice, the Treasury Department, FINCEN, OFAC, FBI, DEA, NDIC, and other agencies involved in drug traffic and money laundering problems. The Justice Department allocated US\$1.85 million of the Forfeiture Assets Fund to the fiscal and customs police, which is the armed body working under the National Tax and Customs Directorate, for the purchase of equipment and training. The funds have not entered Colombia yet, due to problems with the Colombian authorities regarding the legal mechanism for introducing this money specifically bound for the agency selected by the Justice Department.

With the Justice Department, DEA, IRS, and the US Customs Service there is an ongoing joint work to investigate, underveil and prosecute cases of money laundering via the peso broker mechanism, contraband, and tax evasion.

Officials of the US Embassy in Colombia, who are members of the mentioned agencies, work together with DIAN officials on specific cases and Colombian authorities have received all necessary cooperation.

A Joint Task Force is being created, by top-level customs and tax officials of DIAN and by officials of various US Government agencies, such as the Justice Department, Customs, and the IRS. This task force will work on specific investigations leading to unveil contraband, money laundering, and peso brokering cases. The first meeting will take place in Bogotá during the first week of July and will be attended by five officials from the mentioned agencies.

Special mention deserve the Treasury Department, in general, and US Customs, in particular, as well as the Department of Justice. These institutions have collaborated with Colombia in its fight against contraband.

Furthermore, and with the support of the Colombian and US commercial and diplomatic authorities, work is underway to obtain the commitment of multinational companies to control their distribution channels through client knowledge practices, to keep their products from being used to launder money via contraband.

The list of specially designated narcotics traffickers has contributed in the fight against narcotrafficking and could be a useful tool in the fight against contraband as a money laundering facilitator. However, I must indicate that the Colombian Constitutional Court determined that two individuals included on the list, have not being declared guilty of narcotrafficking and ordered the Colombian Administration to inform this situation to the US Administration. The information regarding the individuals or companies that will form part of such list could be more useful if it is maintained at the level of prosecuting offices while the final results of the investigations are issued and the delinquents are declared guilty.

3. Contraband Goods

According to various studies carried out on the subject and to constant seizures by customs authorities, the products subject to contraband are, among others:

- Liquor and alcoholic beverages
- Cigarettes
- Electric and electronic appliances
- Textiles
- Clothing
- Computers
- Automotive parts (where used spare parts constitute a major problem)
- Perfumes
- Jewelry
- Vehicles (including cases of vehicles stolen in Venezuela and the United States)
- Footwear and tennis shoes
- Processed foods
- Chicken parts
- Tires
- Chemical products (among which are chemical precursors) and organic chemical products
- Iron, steel, and their products
- Cement
- Toys
- Rice

- Gasoline along the Venezuelan border
- Semi-trailers

4. The Case of Cigarettes

According to figures from Colombian tobacco manufacturers, between 1991 and 1994, legal imports accounted for 9% of the total cigarettes market; domestic production supplied 33%; and the remaining 58% was accounted for by contraband.

The routes for introducing cigarettes into the country are Aruba and Panama. It has been estimated that if the amount of cigarettes arriving in these two countries were for local consumption, each Panamanian or inhabitant of Aruba, men, women, and children would have to smoke ten packs of cigarettes per day.

The main brand names traded illegally are Marlboro and Belmont, whereby the latter is manufactured in Venezuela by Cigarrería Rigott, under licensing of British American Tobacco. Other brands, such as Kent and Kool, are also traded illegally.

Whereas in 1984, the national cigarette industry supplied 85% of the domestic market, in 1995 this percentage only accounted for a 30% share of consumption measured by volume.

It is estimated that the price per pack to the public is US\$1 dollar and the wholesale price is US\$0.50 with a 50% difference at retail level, contraband profits are estimated to be approximately US\$500 million per year.

Whereas Philip Morris has a price ex works of US\$1.71 per pack, invoices for imports arriving on the Colombian market are for US\$0.24.

5. Liquor Contraband

The contraband of liquor and alcoholic beverages is one of the most sensitive, as the tax structure for these products has a noticeable disturbing effect on the national and departmental tax revenue.

In addition to the existence of a national culture or tradition of liquor contraband, it is considered that this tax structure to which these goods are subjected when imported is the reason that stimulates illegal trade thereof. Liquor in general has a 20% duty, a 40% consumption tax, and a 20%, 25%, and 35% VAT, depending on the alcoholic content of the beverages.

According to estimates of the Colombian Association of Liquor and Wine Importers - ACODIL - in 1997, the total foreign liquor sales in Colombia was 1,475,175 cases, of which 76.3% were accounted for by illegally imported liquor and only 23.7% to legal imports. Of the total number of cases of contraband liquor consumed, the highest percentage is accounted for by whisky with 87.4%, equivalent to 984,200 cases, which compared to 174,143 legally imported cases, gives a clear idea of the magnitude of illegal whisky trade.

The problem of liquor contraband focuses particularly on the major Scotch whisky brands sold by producers in the United Kingdom to distributors in Panama and Aruba.

As in the previously described contraband cases, liquor and cigarettes are believed to be purchased with drug traffic dollars.

6. Place of Origin

It is estimated that 55% of contraband is accounted for by consumer goods (most of which are distributed through Sanandresitos, which are huge malls established in all Colombian cities, where contraband goods are sold openly, violating all customs and tax regulations). Of these goods, 40% come from Panama and Central America; 33% from Ecuador and Venezuela; 13% from North America; 8% from the Far East; and 3% from the Caribbean, mainly Aruba.

7. Colon Free Zone

Most of the articles imported by Colombia from the Colon Free Zone are very similar to those offered in the Sanandresitos. The Panamanian Government has been very reluctant to provide figures regarding re-exports from the Free Zone, but some estimates have been made. In 1997 and 1998, merchandise valued at US\$1.5 and US\$1.2 billion entered Colombia from the Colon Free Zone, and approximately 10% were registered legally, which gives an idea of the magnitude of the contraband problem.

Excluding the Colon Free Zone, imports declared in Colombia as proceeding from Panama amount to US\$70 million, whereas the aforementioned country claims to export only US\$1.3 million in merchandise to Colombia.

Colombia is the main buyer of the Colon Free Zone. Between 1991 and 1995 its share went from 10% to 27% of total purchases originating in this zone.

The Colon Free Zone is the main supplier of merchandise smuggled into Colombia.

8. The Case of "Sanandresitos"

Nowhere in the world is there such an extensive phenomenon as that of *Sanandresitos* in Colombia. They are like an extension of shopping malls, where practically only contraband goods are sold. There are *Sanandresitos* in most Colombian cities. In Bogotá, for example there are more than six large complexes of this type.

The expression "*Sanandresitos*" comes from San Andrés, an island which is a free port. *Sanandresito* sales are estimated to account for 26% of the trade GDP. *Sanandresitos* also sell domestic merchandise, in somewhat over 30% of all sales. In the case of domestically produced merchandise, it has been detected that most of them are manufactured goods with fake brand names.

According to a study performed by Universidad Nacional, in 1996, US\$878 million were laundered through *Sanandresitos*. Gross sales at these centers amounted to US\$2.1 billion, 61% of which (US\$1.2 billion) were accounted for by items illegally smuggled into the country. The sales in these establishments have increased exponentially. In 1985, they accounted for 13.7% of trade GDP, whereas in 1996, the share was 25.6%. Likewise, the area dedicated to this type of business has also increased very rapidly, particularly during the 1990s.

In Bogotá, in 1996, there were 8,571 *Sanandresito* shops. Nation-wide the number of stores was 13,176, of which 11,247 were in business. At present, this type of business begins to be saturated.

In 1978, the number of sales points in Bogotá, Medellín, Cali, Barranquilla, and Bucaramanga, was 2,452. In 1987, in Bogotá alone, there were 2,400 shops. Over the past nine years, the number of *Sanandresito* stores has more than trebled: from 2,400 to 8,571. The physical area occupied by these establishments went from 38,000 square meters in 1985 to 102,853 square meters in 1996, with a significant increase since 1992, of more than 8,000 square meters, to reach a peak of an additional 12,900 square meters in 1995.

As explained earlier, open contraband in the *Sanandresitos* is an important money laundering tool. A business based on contraband, whose main supplier is the Colon Free Zone, where the dollar costs 60% less than the official dollar in Colombia, must necessarily be linked to money laundering. In spite of the seriousness of the problem, Colombian society is permissive vis-à-vis this phenomenon. The fact that *Sanandresitos* are constantly visited by customers shows how the infringement of rules is tolerated. It does not exceed the degree of society's aversion to these illegal activities.

Municipalities grant operating licenses to shopping malls where *Sanandresitos* are established and, even the banks place branches in these areas. DIAN has undertaken an aggressive advertising campaign against *Sanandresitos*, to create an awareness among the population of the fact that buying contraband means taking the jobs away from honest Colombians.

9. Actions Undertaken

As a comprehensive strategy in the struggle against contraband, the need to modernize the customs authority has been identified, in order to achieve more efficient control, while facilitating foreign trade for companies legally established.

Part of the contraband activity may be associated to the difficulties encountered in foreign trade operations, which result from a great deal of red tape in customs processes.

Therefore, work is underway to pass a legal reform that will simplify and expedite procedures related to foreign trade operations.

In addition to the above, the Customs Century XXI computerized system is being developed, which will allow customs procedures to be performed electronically, thus reducing time and cost significantly, and particularly increasing the control of the customs administration. These strategies will enable the establishment of a more efficient customs authority, which will facilitate foreign trade operations following a vision of service, while effectively controlling evasion and contraband. This system has been developed with resources from World Bank.

In this head-on struggle against contraband, the National Government has also developed a series of actions which attempt, in a comprehensive manner, to reduce illegal trade and unlawful competition, while increasing revenue from external taxation. These strategies include:

10. Fiscal and Customs Police Force

One of the most recent measures was the creation and implementation of the Fiscal and Customs Police. This is a police body, under the direction of DIAN, made up of 1,000 men led by a police general, dedicated exclusively to repressing contraband and fighting against tax evasion.

In the same manner as the Antinarcotic Police has succeeded with the support of the US Government in the fight against drug trafficking, we hope to obtain the same level of cooperation to fight contraband, the second stage of this crime.

The Fiscal and Customs Police is an ancillary body to the tax customs and exchange control processes, mainly in regard to the development of strategic operations against evasion, contraband, and infringement of the exchange regulations; the arrest of persons responsible for related crimes, merchandise confiscation, development of intelligence activities, support to the inspection and judicial police duties, and providing the security required in development of certain administrative tasks.

It is hoped that the results in the struggle against contraband will improve substantially with the implementation of this new body, to the extent that there will be controls in many parts of the national territory, where there is no physical presence of customs authorities today, or where there is a need for strengthening the presence of customs authorities, for example the special customs zones. At present, nearly 600 men have joined this group nation-wide, particularly at the most neuralgic ports; and by the end of the first half of the year, the figure will be 1,000 men. They have been properly trained through 3-month seminar-workshops held at the Police Academy, with the participation of DIAN officials.

The US Customs Service, the Justice Department, and DEA have training programs and provide assistance to the Fiscal and Customs Police, which are already taking place or are budgeted and scheduled.

11. Changes on Contraband Penal Types

Contraband and attitudes related therewith were typified as a crime through Law 383 of 1997, in order to make prevention and repression through criminal recourse more effective. In 1998's Tax Reform, contained in Law 488 of December 24, 1988, important changes were introduced, as follows:

- The so-called "personal contraband quota" was reduced from 1,000 to 100 monthly minimum legal wages. In the past, the introduction of contraband merchandise into the country valued at less than US\$153,000 was not considered a crime. Currently, it is not a crime when the price does not exceed US\$15,000. It was not possible to eliminate, once and for all, such a permissive treatment in Congress when this Law was sanctioned.

- Penalties were increased for those favoring contraband, and for officials who contribute to the perpetration of the crime. Penalties for contraband were increased to eight years of imprisonment.

- Contraband has now become a crime, for which no bail can be posted when imprisoned.

12. Currency Exchange Investigation on Contraband Activities

The strategy has been established that whenever the Customs authorities seize contraband goods, a currency exchange investigation is simultaneously initiated, in order to determine the origin of such currency, and to verify compliance with formalities to channel it through the exchange market. From exchange breaches associated with contraband alone, DIAN received US\$10 million in 1998 on account of fines.

13. Creation of a the Financial Information and Analysis Unit

Last week, the Colombian Congress approved the governmental initiative that creates an independent entity in charge of coordinating all activities on preventing and combating money laundering. The unit will contribute to the ongoing work developed by DIAN.

14. Fight Against corruption

One of the main commitments of the current Government is to fight against corruption. The Government has a strategy against corruption known as "de frente al país" or "facing the country". The strategy has two sides: the formation of ethic values and transparency. The strategy involves the participation of the private sector which will be overseeing and commenting on the activities undertaken by the public sector. The central Government has launched a web page www.anticorupcion.gov.co where every citizen can learn about the transparency programs launched by the Government and can denounce practices deemed to be corrupt.

At the international level, Colombia is currently working within the OAS on the cooperation efforts against bribery and is considering joining the OECD Anti-Bribery Convention.

15. Business Polls

The business sector poll carried out by Fedesarrollo and Fenalco is a monthly statistical tool through which the Colombian business sector expresses its opinion on development, evaluation, and current problems of the activity. Among the problems analyzed, it is worth pointing out the following problems of the

sector: supply and sales situation, bank and suppliers credit, supply of domestic and foreign products, and contraband. The attached chart (Schedule I) shows the evolution between 1990 and 1999 (April) of the opinion of polled entrepreneurs in regard to the behavior of contraband as a business problem, measured in terms of the percentage of affirmative answers.

As illustrated in the chart, between January 1990 and mid 1992, a low percentage of businessmen considered this to be a problem, which revealed the lack of importance of contraband as a business issue. The evolution revealed a downward trend. As of that moment, and parallel to the significant increase of imports, following the country's economic liberalization, a noticeable upward trend is evidenced among polled individuals, which reached its peak in December 1995. At that point, 42% of the answers were affirmative, stating that contraband is a major issue.

As opposed to the foregoing, since January 1996, the trend reversed and, month after month, a significant reduction is observed in poll results, up to the point that 35% of the affirmative answers in January 1996 turned to 19% in February 1999, the latter being the lowest figure since May 1995. In March and April 1999, data shows a slight recovery.

16. Colombian Foreign Trade: Measurement of Distortion In Import Figures – 1991 – 1996

This study by the DIAN has complemented a series of studies and research documents developed on contraband and Colombia with quite interesting results and measurements:-

The methodology used and the sources of information consulted allowed to conclude that the total distortion of Colombian imports in 1996 amounted to US\$7.4 billion, of which open contraband, technical contraband and reduced invoicing accounted for a total US\$5.8 billion - equivalent to 78.7% of the total distortion and to 45.3% of total imports, which amounted to US\$12.8 billion that year.

The figures and measurement in this study allow to state that import trade is seriously permeated by illegal practices. Tax duty evasions continues to affect 41% of merchandise introduced into the country, out of a list of goods that ranges from electronic and mechanical appliances to textile products, toys, and recreation items.

The study decisively concludes that smuggled merchandise avoids controls in different ways: at Customs inspections, the goods smuggled amount to US\$2.9

billion; without Customs inspection, the contraband amounts to US\$1.6 billion; and that US\$1.2 billion worth of merchandise entered Colombian territory declaring a lesser purchasing price.

CONCLUSION

Contraband is one of the worst scourges of Colombia's productive sector. It is closely linked to drug-traffic, as it is the most efficient mechanism for money laundering. It corrupts the Customs administration and all of Colombian society.

Customs officials work under constant threat and top officials of the Tax and Customs Administration need body guards. In my case, even my family has protection.

The actions underway seek international cooperation in the struggle against this phenomenon. Here, the response of the U.S. Government has been entirely positive as far as aid, assistance, and cooperation are concerned, as well as in the creation of the Joint Task Force. The Justice Department has offered training for Prosecuting Attorneys who investigate contraband cases and assistance has been provided to those working on money laundering cases. Training is also being requested in areas such as chemical components and illegal drug detection.

Operations in Colombia are guided directly to transport companies that protect contraband, by raiding warehouses established to store the merchandise, and at the level of all foreign trade intermediaries.

The cooperation of multinational organizations in understanding this phenomenon, and in committing in the struggle against all forms of crime described in this document is urgent. It is often claimed that conducting legitimate business in Colombia is difficult as a result of obstacles imposed by Customs authorities to foreign trade transactions. In this context, work is underway to pass a legal reform on Customs procedures, which will simplify paperwork and eliminate obsolete red tape.

In any case, legally established companies conduct their business in Colombia abiding by all regulations in force. There is no reason to believe that some can abide by the law and others can not. It is merely lack of willingness.

Whirlpool Corporation is proof of the fact that good faith in business is possible. They are in the process of signing a compliance agreement with Colombian Customs authorities, in which they commit to not sell their products to distributors in Panama and Florida, whom they know are engaged in contraband activities.

Another company, Daewoo of Korea, has the policy of not selling its products in Sanandresitos. These examples show that multinational companies are aware of the problem and that solutions can be found.

The medium term result should be to eliminate the money laundering mechanism which is an important link in the drug traffic chain.

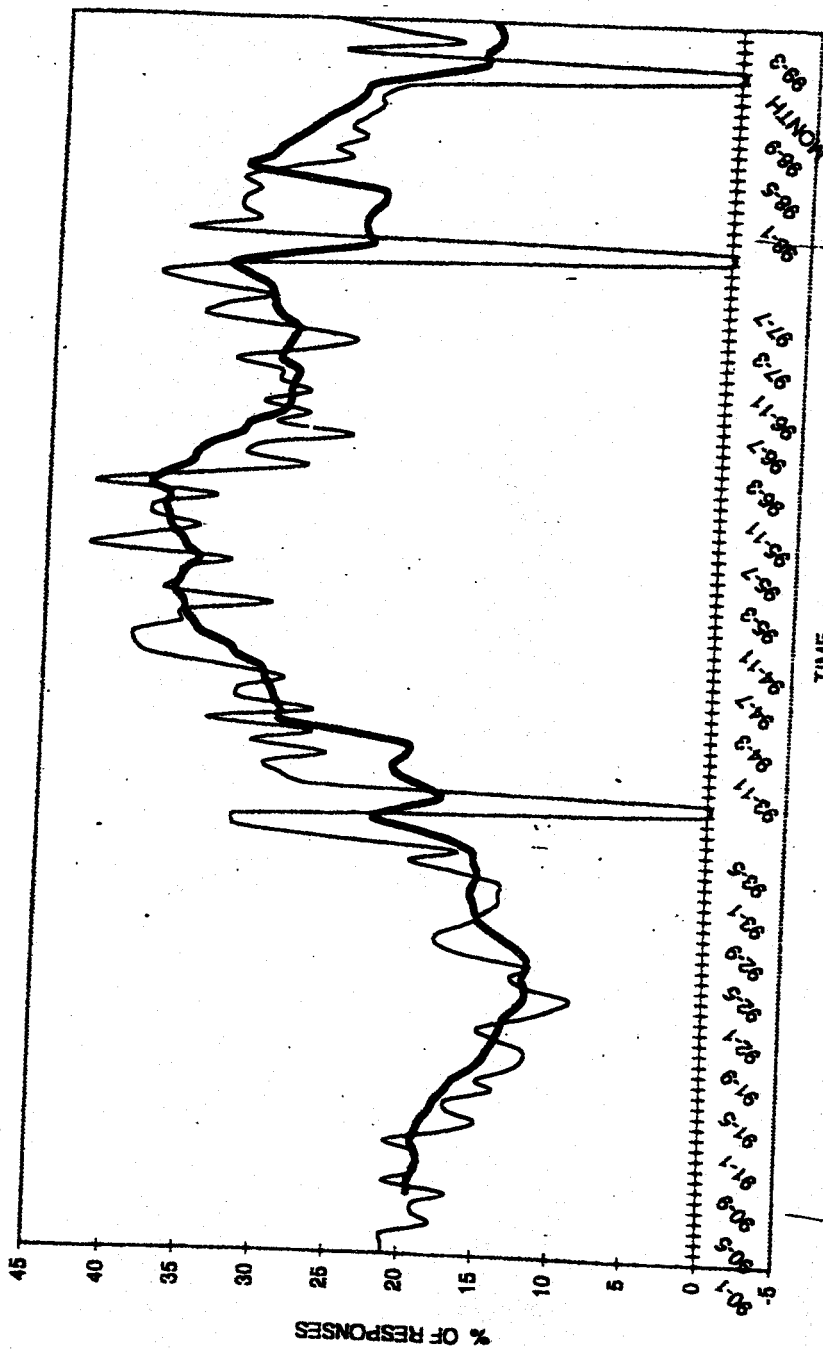
SCHEDULE I
FEDESARROLLO OPINION POLL
CONTRABAND AS A TRADE PROBLEM
1990-1999

MONTH	PERCENTAGE OF RESPONSES
90-1	21
90-2	21
90-3	21
90-4	18
90-5	19
90-6	19
90-7	17
90-8	21
90-9	19
90-10	19
90-11	19
90-12	21
91-1	17
91-2	15
91-3	17
91-4	17
91-5	14
91-6	15
91-7	13
91-8	12
91-9	12
91-10	14
91-11	15
91-12	12
92-1	10
92-2	9
92-3	12
92-4	13
92-5	12
92-6	16
92-7	18
92-8	18
92-9	16
92-10	15
92-11	14
92-12	14
93-1	14
93-2	17
93-3	20
93-4	17
93-5	28
93-6	32
93-7	32

MONTH	PERCENTAGE OF RESPONSES
93-8	27
93-9	28
93-10	30
93-11	28
93-12	31
94-1	27
94-2	34
94-3	27
94-4	32
94-5	32
94-6	29
94-7	33
94-8	38
94-9	39
94-10	39
94-11	36
94-12	36
95-1	30
95-2	37
95-3	36
95-4	36
95-5	33
95-6	42
95-7	39
95-8	35
95-9	38
95-10	38
95-11	34
95-12	42
96-1	35
96-2	28
96-3	32
96-4	31
96-5	25
96-6	30
96-7	28
96-8	31
96-9	28
96-10	30
96-11	30
96-12	33
97-1	28
97-2	25
97-3	29
97-4	35
97-5	34
97-6	31
97-7	35
97-8	36
97-9	31

MONTH	PERCENTAGE OF RESPONSES
97-10	36
97-11	32
97-12	33
98-1	33
98-2	32
98-3	33
98-4	30
98-5	26
98-6	27
98-7	25
98-8	26
98-9	25
98-10	24
98-11	24
98-12	22

OPINION POLL OF FEDESARROLLO
CONTRABAND AS A TRADE PROBLEM
1990-1999



FISCAL COST OF SMUGGLING
1993 - 1998
(Million of Dollars)

CONCEPTS	1993	1994	1995	1996	1997	1998	TOTAL
SMUGGLING (1)	2,613.0	2,812.0	2,771.0	2,275.0	2,683.0	2,328.0	15,462.0
EFFECTIVE DUTY TARIFF (2)	0.0381	0.0295	0.0171	0.021	0.0192	0.0113	
TAX DEFICIENCY COLLECTION	99.6	83.0	47.4	47.8	51.1	28.3	355.1
EFFECTIVE VAT TARIFF (2)	0.1398	0.1396	0.1385	0.159	0.1577	0.1548	
VAT DEFICIENCY COLLECTION	379.2	404.1	390.3	389.3	428.0	384.4	2,335.5
TOTAL DEFICIENCY COLLECTION (TOTAL FISCAL COST)	478.8	487.1	437.7	417.1	479.1	390.8	2,690.6

(1) data estimated in a study prepared for DIAN

(2) corresponds to the annual implicit tariff calculated by O.E.E